

# Changes to Final Fee Disclosure Rule

**U.S. Department of Labor  
Employee Benefits Security Administration  
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The operative language of the final 408b-2 service provider fee disclosure rule (29 CFR §2550.408b-2) reflects certain modifications to the interim final rule (IFR) that was published in the Federal Register on July 16, 2010 (75 Fed. Reg. 41600). The major changes are described below, with citations to the relevant provisions of the final rule.

## **Covered plans – Para. (c)(1)(ii)**

Certain annuity contracts and custodial accounts described in Internal Revenue Code section 403(b) are excluded from the types of pension plans that are covered by the final rule. The excluded contracts and accounts are those which were issued to affected employees before January 1, 2009, where the sponsoring employer ceased making contributions, where rights or benefits of individual owners of the contracts or accounts are enforceable against the insurer or custodian without employer involvement, and where such individual owners are fully vested in benefits provided under the contract or account.

## **Initial Disclosure Requirements – Para. (c)(1)(iv)(C)(2)**

Under the final rule, the information that must be disclosed by a covered service provider (CSP) to a responsible plan fiduciary (RPF) for "indirect compensation," as defined in paragraph (c)(1)(viii)(B)(2), has been enhanced. The initial disclosure requirements contained in paragraph (c)(1)(iv)(C)(2) include a **description of the arrangement made between the payer and CSP,** pursuant to which the indirect compensation is paid. Such descriptions will help a RPF to analyze why the payer is compensating the CSP in connection with the CSP's contract or arrangement with the covered plan.

## **Investment-related Disclosures (fiduciary services) – Para. (c)(1)(iv)(E)**

The final rule adds to the disclosure requirements for descriptions of annual operating expenses (e.g., expense ratio) of a "designated investment alternative" (DIA). The final rule requires disclosure of **total annual operating expenses (TAOE)** for DIAs, expressed as a percentage, **calculated in accordance with the Department's new regulations at 29 CFR §2550.404a-5(h)(5), which involve disclosures that must be made to participants** in participant-directed individual account plans (the "P-level" disclosure regulation). In addition, the final rule requires disclosure of any other information relating to DIAs that is within the control of, or reasonably available to, the CSP, if the information is considered investment-related information which must be provided automatically under the P-level regulation (29 CFR §2550.404a-5(d)(1)). These changes are designed to facilitate disclosure of information under both the 408b-2 and P-level regulations.

## **Investment-related disclosures (record-keeping / brokerage services) – Para. (c)(1)(iv)(F)**

The final rule changes the focus of the so-called "pass-through" relief provided in the IFR for disclosures of investment-related information. CSPs may now comply with requirements for investment-related disclosures relating to DIAs by providing current disclosure materials of the issuer of the DIA, or information replicated from such materials. In such instances, the "issuer" of the DIA must be one of the following entities: (i) a registered investment company (i.e., mutual fund); (ii) an insurance company qualified to do business in a State; (iii) an issuer of a publicly-traded security; or (iv) a financial institution supervised by a State or Federal agency. The final rule's provisions no longer focus on whether the disclosure materials themselves are regulated but rather on whether the institution issuing the materials is regulated. In addition, the CSP must act in good faith, must not know that the materials are incomplete or inaccurate, and must state that it makes no representations as to the completeness or accuracy of such materials.

## **Guide to Initial Disclosures – Para. (c)(1)(iv)(H)**

The final rule reserves a place for the future development of provisions that would require the CSP to separately furnish a guide or similar tool designed to enable the RFP to locate compensation information disclosed through multiple or complex documents. The preamble to the final rule states that the Department intends to soon publish in the Federal Register a Notice of Proposed Rulemaking on this matter. Meanwhile, the Department has included a **Sample Guide** as an appendix to the final rule to encourage service providers to assist plan fiduciaries with their review of required disclosures.

## **Timing of Initial Disclosures; changes – Para. (c)(1)(v)(B)(2)**

The final rule changes the deadline for disclosures of all investment-related information to "**at least annually.**" The IFR had previously required that such information be disclosed within 60 days. The deadline for disclosure of changes to other information that has been previously disclosed remains 60 days from the date a CSP is informed of such change.

## **Reporting & Disclosure (R&D) information; timing – Para. (c)(1)(vi)(B)**

The deadline for providing R&D information to a RPF upon request has changed under the final rule. The information must now be provided to the RPF "reasonably in advance of the date upon which" such RPF or covered plan administrator "...states that it must comply with" applicable R&D requirements.

## **Disclosure Errors – Para. (c)(1)(vii)**

The final rule clarifies that disclosure of "changes" to information previously disclosed is covered by the "error disclosure" provision. Thus, errors or omissions in disclosures of "changes" to previously disclosed information can be corrected as well within 30 days after the CSP knows of the error or omission.

## **Definitions – Para. (c)(1)(viii)(B)**

The final rule adds to the definition of "compensation" in paragraph (c)(1)(viii)(B), clarifying descriptions that may be made of compensation or cost, as expressed by monetary amounts, formulas, percentages, per capita charges, or other reasonable methods. The definition, as modified, allows for a "reasonable and good faith" estimate of compensation or cost if the CSP cannot otherwise readily describe the compensation or cost (paragraph (c)(1)(viii)(B)(3)). In such instances, the CSP must explain the methods and assumptions used for the estimate.

## **Exemption for RPF – Para. (c)(1)(ix)(G)**

The final rule changes the language of one of the conditions required for relief under the class exemption. The exemption states that a RPF, upon discovering that a CSP has failed to disclose certain information, must request the information in writing from the CSP. Under the final rule, if a CSP fails to comply with the written request within 90 days, the RPF must determine whether to terminate or continue the contract or arrangement "...consistent with its duty of prudence under section 404..." If the information relates to future services and is not disclosed promptly after the 90-day period, the final rule requires that the RPF must terminate the service arrangement "...as expeditiously as possible," consistent with its duty of prudence. This change highlights the importance of prompt decision-making by a RPF regarding the termination of a service arrangement when disclosure failures have occurred.

## **Effective Date – Para. (c)(1)(xii)**

The final rule's effective date has been extended to July 1, 2012, to allow additional time for compliance.

For a more complete discussion of the major changes noted above, interested persons are directed to the explanations contained in the preamble to the final rule, as published in the Federal Register.

## Recap

### ***Covered plans – Para. (c)(1)(ii)***

Certain annuity contracts and custodial accounts described in Internal Revenue Code section 403(b) are excluded from the types of pension plans that are covered by the final rule.

### ***Initial Disclosure Requirements – Para. (c)(1)(iv)(C)(2)***

The initial disclosure in paragraph (c)(1)(iv)(C)(2) must include a description of the arrangement made between the payer and CSP, pursuant to which the indirect compensation is paid.

### ***Investment-related Disclosures (fiduciary services) – Para. (c)(1)(iv)(E)***

The final rule requires disclosure of total annual operating expenses for designated investments, expressed as a percentage, that is consistent with participant disclosure requirements (29 CFR §2550.404a-5(h)(5), – Para. (c)(1)(iv)(F)).

### ***Guide to Initial Disclosures – Para. (c)(1)(iv)(H)***

The Department has included a Sample Guide as an appendix to the final rule to encourage service providers to assist plan fiduciaries with their review of required disclosures.

### ***Timing of Initial Disclosures; changes – Para. (c)(1)(v)(B)(2)***

The final rule changes the deadline for disclosures of all investment-related information to "at least annually."

### ***Reporting & Disclosure (R&D) information; timing – Para. (c)(1)(vi)(B)***

The deadline for response to a request for information from a plan fiduciary is "reasonably in advance of the date upon which" the plan fiduciary "...states that it must comply with" applicable requirements.

### ***Disclosure Errors – Para. (c)(1)(vii)***

Errors or omissions in disclosures of "changes" to previously disclosed information can be corrected within 30 days after the CSP knows of the error or omission.

### ***Definitions – Para. (c)(1)(viii)(B)***

If the CSP cannot readily describe the compensation or cost (paragraph (c)(1)(viii)(B)(3)) the CSP must explain the methods and assumptions used for the estimate.

### ***Exemption for Plan Fiduciary – Para. (c)(1)(ix)(G)***

Under the final rule, if a CSP fails to comply with the written request within 90 days, the plan fiduciary must determine whether to terminate or continue the contract or arrangement "...consistent with its duty of prudence under section 404..." If the information relates to future services and is not disclosed promptly after the 90-day period, the final rule requires that the plan fiduciary must terminate the service arrangement "...as expeditiously as possible," consistent with its duty of prudence. This change highlights the importance of prompt decision-making by a plan fiduciary regarding the termination of a service arrangement when disclosure failures have occurred.

### ***Effective Date – Para. (c)(1)(xii)***

The final rule's effective date has been extended to July 1, 2012, to allow additional time for compliance.