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# Mastering the New EBSA Rules on Covered Plan Fee and Expense Reporting

Ensuring That 401(k) and 403(b) Plans Make Complete and Timely Disclosures

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WEDNESDAY, OCTOBER 26, 2011

1pm Eastern | 12pm Central | 11am Mountain | 10am Pacific

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Today's faculty features:

Stanley Baum, Counsel, Lerner Law Firm & Associates, Westbury, N.Y.

Kelly Pointer, Seyfarth Shaw, New York

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# Mastering the New EBSA Rules on Covered Plan Fee and Expense Reporting Seminar

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Oct. 26, 2011

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# Today's Program

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Material Terms Of Final EBSA Rules  
*[Kelly Pointer and Stanley Baum]*

Slide 7 - Slide 31

Impact Of Fiduciary Rules Related To EBSA  
*[Kelly Pointer]*

Slide 32 - Slide 34

Steps To Prepare Now For New Disclosure Requirements  
*[Stanley Baum]*

Slide 35 - Slide 41

Kelly Pointer, Seyfarth Shaw

Stanley Baum, Lerner Law Firm & Associates

# **MATERIAL TERMS OF FINAL EBSA RULES**

# Goals Of Fee Disclosure Regulations

- Help participants invest their accounts
  - Information in one place
  - Improved investment results
- Transparency as to investment alternatives
  - Increased competition, drive down fees
  - Effects of fees and expenses on account balance
- Information about plan features that affect account balance



# Who Gets The Disclosures?

- Participants
  - All employees eligible to participate, even if not enrolled
    - Serve as reminder of eligibility to participate
- Beneficiaries
  - Beneficiaries that can direct the investment of assets in their accounts
    - E.g., due to participant's death, QDRO
- No exception for small plans

# Categories Of Disclosure

Two general categories

- Plan features
  - The financial aspects of plan features and administrative expenses
- Investment disclosures
  - E.g., performance, fees and expenses, benchmarks
- Not required to be all in one document
  - Combination of annual disclosure, quarterly statements and SPD

# Plan Features

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- When and how investment instructions can be given
- Any limitations on those rules
  - Whether imposed by the plan or the investment alternative
- Plan provisions for voting, tender and similar rights
  - E.g., pass-through voting

# Plan Features: Expenses Shared By All

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- What expenses are chargeable in theory
  - Not specific to one participant
  - Administration (e.g., legal or accounting fees)
- What actually was charged that quarter
- Whether any of the expenses were paid with revenue-sharing dollars

# Plan Features: Individual Expenses

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- What expenses are chargeable in theory
  - Specific to one participant
  - Two types
    - Plan administration (e.g., loan processing fees)
    - Investment-related (e.g., commissions or sales loads) for investing in any of the investment alternatives
- What actually was charged that quarter

# Investment Disclosures: All Funds

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- For all investment alternatives (fixed or variable):
  - Name and type
- Shareholder-type fees
  - E.g., sales loads and surrender charges
  - (Also covered in “plan features - individual expenses” previously)
- Restrictions on purchase, transfer or withdrawal
  - E.g., trading frequency
- Any investment managers

# Investment Disclosures: Variable Return

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- For each investment alternative with a variable return:
  - Past performance
    - One-, five- and 10-year, if available
    - Benchmark identification and performance
  - Annual operating expense
    - Percentage and dollar-per-thousand
    - Chart format allows an easy, side-by-side comparison.

# Investment Disclosures: Fixed Return

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- For each investment alternative with a fixed return:
  - Rate of return
  - Term of investment
  - If the issuer can adjust the rate of return during the term
    - Statement disclosing such right
    - Any minimum guaranteed rate
    - How to obtain the current rate



# Include Reminders For Participants ...

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- Three statements must be included
  - Past performance is not necessarily indicative of future performance.
  - Fees are only one item to consider when selecting investments.
  - Fees and expenses can substantially reduce account growth, with reference to EBSA's Web site for an example of the long-term effects of fees and expenses.
    - [http://www.dol.gov/ebsa/publications/401k\\_employee.html](http://www.dol.gov/ebsa/publications/401k_employee.html)

# Online And Available On Request

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- On the Internet
  - Each investment alternative must reference a Web site with the alternative's:
    - Name of issuer
    - Objectives or goals
    - Principal strategies and risks, with general description of assets
    - Turnover rate (how frequently it buys and sells securities)
    - Performance data (same data as described above)
    - Shareholder-type fees and annual operating expenses (same data described above)
    - Glossary of investment terms (cross-reference is OK)
  - Paper copies available without charge

# Online And Available On Request (Cont.)

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- On request:
  - If registered, the investment alternative’s prospectus
  - Financial statements or reports that are provided to the plan
  - Share or unit price, and date of such valuation
  - List and proportion of the assets comprising the investment alternative, to the extent they are “plan assets”

# Special Rules: Brokerage Windows

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Brokerage windows not considered investment alternatives for this purpose, but disclosure is still required of fees and expenses charged to use the brokerage window.

# Special Rules: Employer Stock

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- On the Web site
  - Replace “principal strategies and risks” with a statement explaining the importance of a well-balanced and diversified investment portfolio
    - Department of Labor published model language in 2006.
  - Turnover rate is not required.
  - “Annual operating expense” is required only if fund is unitized.
- On the annual notice
  - “Annual operating expense” is required only if fund is unitized.
  - Alternative method of calculating performance (for one-, five- and 10-year periods), if fund is not unitized

# Special Rules: Annuities

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- Alternative annual disclosure
  - Instead of the investment disclosures listed previously, provide:
    - Name of contract, fund or product
    - Objectives or goals
    - Benefits, and factors that determine the price of the payments
    - Limitations on withdrawal or transfer amounts allocated to the option (e.g., lock-up), and any related fees or charges
    - Any fees reducing the contribution to the product, e.g., surrender charges or administrative fees
    - A statement that guarantees of an insurance company are subject to long-term financial strength and its ability to pay claims

# Special Rules: Annuities (Cont.)

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- Alternative Internet disclosure
  - The Web site for an annuity must provide:
    - Name of issuer and of contract or product
    - Objectives or goals
    - Forms of distribution (e.g., payments for life, a specified term)
    - Costs or factors taken into account in determining the price of benefits
    - Any fees reducing the contribution to the product, e.g., surrender charges or administrative fees

# Timing And Manner Of Fee Disclosures

1. The plan administrator (PA) or its designee will provide the fee disclosures.
2. Plan-related information must be disclosed. This information:
  - a) Must be based on the latest info available to the plan
  - b) Must be provided:
    - On or before the date on which a participant or beneficiary can first direct the investments in his or her plan accounts, and at least annually thereafter
    - If there is a change in the information, each participant and beneficiary must be given a description of this change at least 30 days, but not more than 90 days, in advance of the change's effective date. However, when the PA is unable to meet that time frame due to events that are unforeseeable or beyond the PA's control, notice of such change must be furnished as soon as reasonably practicable.



## **Timing And Manner Of Fee Disclosures (Cont.)**

3. The following information must be provided quarterly:
  - a) Information on plan-wide administrative expenses and individual expenses actually charged to the account of a participant or beneficiary
  - b) Information on the services resulting in the charges in (a)
  - c) A disclosure that designated investment alternatives have administrative and other operating expenses charged against their own assets
  
4. Investment-related information (the DOL chart):
  - a) Must be based on the latest information available to the plan
  - b) Must be provided on or before the date on which a participant or beneficiary can first direct the investments in his or her plan account, and at least annually thereafter

## **Timing And Manner Of Fee Disclosures (Cont.)**

5. So now, we have initial, annual and quarterly disclosures. The initial disclosure (consisting of plan-related information and investment-related information) must be made by the later of:
  - a) The 60<sup>th</sup> day after the start of the first plan year to begin after Oct. 31, 2011; or
  - b) May 31, 2012.

This will be May 31, 2012 for a calendar-year plan.

6. The first quarterly disclosure must be made by the 45<sup>th</sup> day after the end of the calendar quarter in which the first initial disclosure is made.

This will be Aug. 14, 2012 for a calendar-year plan.

7. Thereafter, for the later annual disclosures, “annually” means at least once during any 12-month period.

For the later quarterly disclosures, “quarterly” is at least once during any three-month period.

## **Timing And Manner Of Fee Disclosures (Cont.)**

8. How should the PA make the initial, annual and quarterly disclosures?
  - a) The PA can always make them in standalone documents.
  - b) The initial and annual disclosures of plan-related information can be included in either the plan's summary plan description (the SPD), or in the quarterly benefit statement required under Sect. 105 of ERISA, added by the 2006 Pension Protection Act (this will require revision of the SPD or benefit statement). But, this is permitted only if the SPD or quarterly benefit statement is given out by time the disclosure is otherwise required.
  - c) The quarterly disclosure (generally of expenses charged to the participant and beneficiary accounts) can be included with the quarterly benefit statement (this will require revision of that statement).

## **Timing And Manner Of Fee Disclosures (Cont.)**

9. Medium of disclosure. The PA can always provide the disclosure as a hard copy. The PA can also provide the disclosure through electronic medium, by following Technical Release 2011-03. The Technical Release offers three alternatives:

The first alternative: Use the Department of Labor's "safe harbor" for electronic delivery under 29 CFR 2520.104b-1(c). Under the safe harbor, information may be disclosed by electronic media if:

- a) Proper notice is given along with the disclosure.
- b) The PA takes steps to ensure actual delivery of the information being disclosed.
- c) The PA takes steps to protect the confidentiality of personal information pertaining to plan accounts.
- d) The disclosure is presented in an appropriate form.
- e) The intended recipient either:
  - Has access to the electronic media at work, and access to it is an integral part of his or her work duties
  - Gives affirmative consent to electronic media use

# Timing And Manner Of Fee Disclosures (Cont.)

The second alternative: This is generally intended to be used when there is no access to electronic media at work. Under this alternative, disclosures may be delivered by electronic media if the following requirements are met:

- a) The PA provides initial notice of electronic media delivery. This notice describes:
  - i. The specific information to be disclosed
  - ii. The recipient's right to request a paper copy of the information
  - iii. That the recipient may decline, or at any time opt out of, this type of delivery
  - iv. That an e-mail address must be provided voluntarily by the recipient
  - v. The procedures for the recipient to furnish and update the e-mail address
- b) The recipient voluntarily provides his or her e-mail address.
- c) The PA provides annual notices, with generally the same info as initial notice.
- d) The PA take steps to ensure the actual delivery of the disclosure and maintenance of the recipient's confidential personal information.

There is a transitional rule under which the PA can use an individual's e-mail address on file to meet the "voluntary provision" rule.

## **Timing And Manner Of Fee Disclosures (Cont.)**

The third alternative: For information that the PA chooses to disclose with the quarterly pension benefit statement, the PA can use Field Assistance Bulletin 2006-03. Under this alternative, the PA can provide the disclosures through electronic media by:

- a) Following the safe harbor in 29 CFR 2520.104b-1(c) discussed previously,
- b) Following the IRS rules for electronic provision of qualified plan notices in Treas. Reg. Sect. 1.401(a)-21, or
- c) Providing disclosure on a secure Web site, if certain notice requirements are met

# Timing And Manner Of Fee Disclosures (Cont.)

10. If a participant or beneficiary requests such, the PA must provide supplemental information about each of the plan's designated investment options, including as to each option:
  - The prospectus
  - Financial statements and shareholder reports, if made available to the plan
  - Share values, and assets held by the investment and their value
11. The PA must provide a Web site sufficiently specific to provide participants and beneficiaries with the following information (generally prepared in accordance with SEC rules) on each designated investment option:
  - Name of issuer
  - Performance data (same as the chart), updated at least quarterly
  - Investment issuers' objectives, investment strategies, risks, turnover rate, and fees and expenses

The regulations require the PA to provide a glossary. It will consist of terms needed to understand the plan's designated investment options, and probably has to be included in the Web site.

12. If the plan passes through voting and similar rights, the PA must pass through (to the extent furnished to the plan, and to any participants and beneficiaries investing in an investment option) materials on voting, tender and similar rights for that option.

Kelly Pointer, Seyfarth Shaw

# **IMPACT OF FIDUCIARY RULES RELATED TO EBSA**



# Overlap With ERISA 404(c) Plans

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- Fee disclosure regulations address participant investment responsibility, but do not address results of participants' investment choices.
- ERISA Sect. 404(c) alleviates fiduciaries from responsibility for investment results.
  - Disclosures generally the same
  - Must also have SPD designation as 404(c) plan
  - Other parameters must be met for 404(c) compliance
    - E.g., frequency of trading, diverse menu of investment alternatives

# Fiduciary Responsibility

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- Providing the plan and investment disclosures is a fiduciary responsibility.
  - However, performance of the tasks likely will be delegated to an administrator.
  - As fiduciary is still responsible, it might be advisable to monitor the process.
- Data for disclosures will, in many cases, come from third parties (e.g., service providers, issuers of designated investment alternatives).
  - No fiduciary liability under the regulations, if reliance in good faith
- Although participants direct investments, there is no change to fiduciary responsibility to prudently select and monitor the designated investment alternatives.

Stanley Baum, Lerner Law Firm & Associates

# **STEPS TO PREPARE NOW FOR NEW DISCLOSURE REQUIREMENTS**

# **Action By The Plan Administrator (PA)**

1. The PA should become familiar with the DOL model comparative chart and the particular information for his or her plan. Participants will have questions about the performance and expenses. Start thinking through potential questions and answers. Be ready to make changes in the investments offered.
2. When thinking about changes, the PA need not select the service provider or investment option with the lowest fees. Consider:
  - For a service provider, the type and amount of services provided, how long the provider has been in business and serving the plan, and the PA's and participants'/beneficiaries' satisfaction and problems with services previously provided
  - For an investment option, consider the risk and return, how the investment fits into the plan's portfolio, the age of the investment and the competence and tenure of its management.
3. Take care not to overload participants and beneficiaries. In particular, consider revising SPDs and other plan communications, cutting down the number of designated investment alternatives and educating participants about the new disclosures.

## **Action By The Plan Administrator (PA), Cont.**

4. The PA should start talking to the plan's designated investment issuers. Make sure they can compute and give the PA the investment-related information, and as applicable, the plan-related information (e.g., they may be performing and charging for recordkeeping and other administration). Some of the information on performance and expenses must be prepared in accordance with SEC rules, with which those entities are familiar.
5. Under the regulations, the PA can rely on the information provided by service providers, as long as this reliance is reasonable and in good faith.
6. If the plan has one designated investment issuer (e.g., all investments through Fidelity), then that issuer can probably prepare the chart for the PA. If the plan has multiple designated investment issuers, either a third-party administrator, another service provider or someone in-house must coordinate the information and actually prepare the chart.
7. In particular, the PA should talk to designated investment issuers, and if needed the plan's other service providers, about setting up the required Web site and procedures for updating it quarterly.

## **Action By The Plan Administrator (PA), Cont.**

8. A 403(b) plan may have problems here. Its investment issuers could be all over the country and beyond. In general, under the 403(b) regulations, the PA has to identify all investments and their issuers, so that all investments are part of a written plan. Now, the PA must make these identifications to comply with these fee disclosure regulations.
9. Under the regulations, the PA must make the disclosures to the following individuals: Any participant with an account balance, any participant's beneficiary or alternate payee under a QDRO with an account balance, AND any employee who is eligible to make contributions. The PA must act now to begin identifying all of these individuals, so that it can make the required disclosures.
10. The PA must develop procedures and deadlines for providing the initial, annual and quarterly disclosures. There is an affirmative requirement to provide the disclosures. The PA cannot simply ask participants and beneficiaries to get information online (as is done currently).
11. The PA must identify and budget for all costs of accumulating the required information and carrying out the procedures for disclosure.

## **Action By The Plan Administrator (PA), Cont.**

12. The PA should consider the consequences of not making the disclosures required by the regulations, as follows:
- a) The Department of Labor apparently believes that, under Sect. 404(a) of ERISA, a PA must take steps to ensure that, on a regular and periodic basis, participants and beneficiaries are made aware of their rights and responsibilities over plan investments held in their accounts, and are provided with sufficient information about those investments to make informed decisions.
  - b) If the PA does not meet the disclosure rules as set out in the regulations, the PA is likely to fail to meet the Department of Labor's interpretation of Sect. 404(a), as set out in (a) above.
  - c) There is no statutory penalty for the failure in (b), but the failure could lead to:
    - A breach of fiduciary duty under ERISA Sect. 404(a)(1)(A) and (B)
    - Personal liability for participant losses
    - A growing list of equitable remedies leading to injunctive relief and/or monetary outlay.

## **Action By The Plan Administrator (PA), Cont.**

13. The PA should not forget the service provider disclosure rules. The ERISA Sect. 408(b)(2) regulations (29 C.F.R. Sect. 2550.408b-2(c)) require that service providers give the plan information about their services and fees.
  
14. Those disclosure begin to apply on April 1, 2012. That date, and the May 31 initial disclosure date for the plan and investment-related information are not coincidence. The Department of Labor anticipates that the fee information required by April 1 will be used in making the May 31 disclosure. The PA must coordinate compliance efforts for 408(b)(2) regulations and the participant fee disclosure rules.



## **Action By The Plan Administrator (PA) Cont.)**

15. Which service providers must give fee and service info under the 408(b)(2) regulations? It is any service provider that enters into a contract or arrangement with a plan (with expected fees of at least \$1,000 (over what period?), and that is:
- a) A fiduciary for ERISA purposes, including the fiduciary of a designated investment option consisting of plan assets. This fiduciary has plan-related information and, maybe, investment-related information.
  - b) An investment adviser to the plan. This adviser may have investment-related information.
  - c) A provider of recordkeeping or brokerage services, which covers at least one of the plan's investment options. This provider has plan-related information.
  - d) A provider receiving indirect compensation (not received directly from the plan, the plan sponsor, or a service provider or affiliate, but ultimately charged to the plan) for the following services: consulting, accounting, auditing, recordkeeping, actuarial, legal, securities or other investment brokerage, appraisal, valuation, banking, custodial, insurance, third-party administration and investment advisory (for participants). This provider has plan-related information and, maybe, investment-related information.