



# Pension Analyst

Important information

Plan administration and operation

December 2010

## DOL issues final participant fee disclosure rules for defined contribution plans

### Who's affected

This rule applies to plan administrators of participant-directed defined contribution plans (including 403(b) plans) that are subject to ERISA. This rule does not apply to governmental plans, church plans that do not elect to be covered by ERISA ("nonelecting church plans"), or non-ERISA 403(b) plans.

### Background and summary

Under ERISA, plan fiduciaries are required to act prudently and solely in the interest of participants and beneficiaries. In plans where participants and beneficiaries have investment responsibility for their accounts, fiduciaries must ensure participants and beneficiaries have adequate information to make informed decisions about the management and investment of their retirement savings.

On October 20, 2010, the Department of Labor (DOL) issued final rules requiring disclosure of fees, expenses, and other plan and investment-related information to participants and beneficiaries in participant-directed defined contribution plans that are subject to ERISA. The final rules establish uniform, basic disclosures for participants and beneficiaries, regardless of whether the plan intends to comply with voluntary ERISA section 404(c). These rules require certain plan and investment-related information to be provided on or before the first date the participant or beneficiary can direct his or her investments and annually thereafter. Administrative and individual expenses actually charged to a participant must be disclosed quarterly. In addition, other materials, such as prospectuses and financial reports must be provided upon request, and certain material must be provided on a website.

These rules apply to plan years beginning on or after November 1, 2011 (e.g., January 1, 2012 for calendar year plans). Initial disclosures must be provided to existing participants and beneficiaries within 60 days of the first plan year beginning on or after November 1, 2011.

### Action and next steps

Employers that sponsor defined contribution plans subject to ERISA that allow participants and beneficiaries to direct the investments in their account should familiarize themselves with these rules. Plan administrators of affected plans must provide the disclosures in a timely manner to satisfy their fiduciary duties under ERISA.

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## Overview

The DOL believes fiduciaries of participant-directed defined contribution plans must take steps to ensure participants and beneficiaries, on a regular and periodic basis, are aware of their rights and responsibilities for investing account assets. DOL further believes that plan fiduciaries must ensure participants and beneficiaries are provided sufficient information regarding the plan, and designated investment alternatives available under the plan, including related fees and expenses, so they may make informed decisions regarding the management of their plan accounts.

The final participant fee disclosure rules require plan fiduciaries to ensure participants and beneficiaries are provided with certain information regarding plan-related information, as well as investment-related information. A summary of some of the key requirements is provided below. For purposes of these rules, the definition of “participants” includes employees who are eligible to participate under the terms of the plan, regardless of whether the employee has chosen to participate. The definition of “beneficiary” includes beneficiaries who have a right to direct investments of their account following the death of a participant or under a qualified domestic relations order (i.e., alternate payees).

## Plan-related information

The final rules require disclosure of plan-related information in three categories: general plan information, administrative expense information, and individual expenses information. Certain plan-related information must be provided on or before the first date participants and beneficiaries can direct their investments, and annually thereafter. These disclosure requirements may be satisfied by furnishing the most recent annual disclosures, along with any updates made to these disclosures. Other plan-related information must be provided quarterly.

If any of the plan information changes, a description of the change must be furnished to participants and beneficiaries at least 30 days, but not more than 90 days, before the effective date of the change. However, there may be times where the changes must be made within a time frame that would preclude compliance with the 30-day advance notice requirement (e.g., elimination of an investment option when it is determined to no longer be a prudent investment alternative). In those cases, the information must be furnished as soon as reasonably practicable.

### General plan information

On or before the date they can first direct their investments, and at least annually thereafter, participants and beneficiaries must be provided:

- An explanation of the circumstances under which they may give investment instructions;
- An explanation of any specified plan-imposed limitations on investment instructions, including any restrictions on transfers to or from designated investment alternatives;
- A description or reference to plan provisions relating to the exercise of voting, tender, and similar rights and any restrictions on those rights;
- A list of investments offered under the plan;
- Identification of investment managers; and
- A description of any “brokerage windows,” “self-directed brokerage accounts,” or similar plan arrangements that enable participants and beneficiaries to select investments beyond those designated by the plan.

This information may be included in the summary plan description (SPD) or benefit statement, if timing requirements can be met.

### Administrative expenses

On or before the date they can first direct their investments, and at least annually thereafter, participants and beneficiaries must also be provided an explanation of any fees and expenses for general plan administrative services (e.g., legal, recordkeeping, accounting services) that may be charged against their individual accounts (whether by liquidating shares or deducting dollars), and on the basis on which such charges will be allocated (pro rata, per capita). This information may be included in an SPD or benefit statements if timing requirements can be met.

In addition, participants and beneficiaries must be provided a statement at least quarterly that includes the dollar amount of the administrative fees and expenses that are actually charged (whether by liquidating shares or deducting dollars) to their accounts during the preceding quarter. This statement must also include a description of the services to which the charges relate (e.g., plan administration, recordkeeping, legal, accounting services). If applicable, the statement must include an explanation that, in addition to fees and expenses disclosed in the quarterly statement, some of the plan's administrative expenses for the preceding quarter were paid from the total operating expenses of one or more of the plan's designated investment alternatives (e.g., through revenue sharing arrangements, 12b-1 fees, subtransfer agent fees). This information may be included on the plan's quarterly benefit statement if timing requirements can be met.

### Individual expenses

On or before the date they can first direct their investments and at least annually thereafter, participants and beneficiaries must be provided an explanation of any fees and expenses that may be charged against their accounts on an individual basis, and which are not reflected in the total annual operating expenses of any designated investment alternative. Examples of these individual expenses include loan processing fees, QDRO fees, 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. This information may be included in an SPD or benefit statements if timing requirements can be met.

In addition, participants and beneficiaries must be provided a statement at least quarterly that includes the dollar amount of individual fees and expenses that are actually charged (whether by liquidating shares or deducting dollars) to their accounts during the preceding quarter. This statement must also include a description of the services to which the charges relate (e.g., loan processing fees). This information may be included on the plan's quarterly benefit statement if timing requirements can be met.

### Investment-related information

Participants and beneficiaries must be provided certain investment-related information in a comparative format on or before the date they can first direct their investments and at least annually thereafter. The DOL has provided a [model comparative chart](#) that may be used to satisfy this disclosure requirement. Plan administrators may either use the model comparative chart or create their own chart or similar format.

Brokerage windows, self-directed brokerage accounts, and similar arrangements are not considered to be designated investment alternatives subject to these rules.

### Identifying information

The following identifying information must be included with respect to each designated investment alternative offered under the plan:

- Name of each designated investment alternative;
- 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).

### Performance data

For designated investment alternatives that have a variable rate of return, the plan administrator must provide the average annual total return of the investment for 1-, 5-, and 10- calendar year periods, (or for the life of the investment, if shorter) ending on the date of the most recently completed calendar year. The disclosure must also include a statement indicating that an investment's past performance is not necessarily an indication of how the investment will perform in the future.

For investments not registered under the Investment Company Act of 1940, the final rules allow a plan administrator to use a reasonable estimate of expenses if he reasonably determines there is not enough information on expenses to calculate the 5- and 10-year average annual total returns. This transition relief applies to plan years beginning before October 1, 2021.

For designated investment alternatives that have a fixed or stated return (e.g., GIC, CD, variable annuity fixed account), the plan administrator must provide both the fixed or stated annual rate of return and the term of the investment. If the issuer of the investment has the right to adjust the rate of return during the term of the contract or agreement, the disclosure must include 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.

It is important to note that according to the preamble to these regulations, stable value and money market funds are *not* considered to be fixed return investments.

### **Benchmarks**

For investments that have a variable rate of return, the disclosure must include the name and returns of appropriate broad-based securities market index over the 1-, 5-, and 10- calendar year periods (or for the life of the investment, if shorter). The index must not be one administered by an affiliate of the investment issuer, its investment adviser, or a principal underwriter, unless the index is widely recognized and used.

### **Fees and expense information**

For investments that have a variable rate of return, the following information must also be provided:

- 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);
- The total annual operating expenses of the investment expressed as a percentage (i.e., expense ratio);
- An example illustrating the effect of the annual operating expenses of the investment for a one-year period, expressed as a dollar amount for a \$1,000 investment;
- A statement that fees and expenses are only one of several factors that participants and beneficiaries should consider when making investment decisions;
- A statement that past performance is not necessarily indicative of future performance; and
- 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 (EBSA) website for an example.

For investments that have a fixed return 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 any portion of the investment.

### **Additional investment-related information**

The investment-related disclosure must provide an internet website address for each investment that provides participants or beneficiaries additional specific investment information including:

- The name of the issuer;
- The investment's objectives;
- The principal strategies and risks;
- The portfolio turnover rate for variable investments, as appropriate;
- Performance data updated at least quarterly; and
- Fee and expense information.

The website address cannot simply direct the participant or beneficiary to the investment issuer's home page.

The investment-related disclosure must also include a glossary of terms to assist participants and beneficiaries in understanding the investments, or an Internet website address that provides access to a glossary, along with a general

explanation of the purpose of the address.

In addition, the final rules contain a special rule for annuities which provides that in place of the investment-related information described [above](#), the plan administrator must provide each participant and beneficiary with basic information about the benefits and costs of the annuity, including the annuity option's objectives, factors that determine the price of the guaranteed income payments, any limitations on a participant's or beneficiary's ability to withdrawal or transfer amounts allocated to the option, any fees or charges applicable to the withdrawal or transfers, and any fees that will reduce the value of amounts allocated. The annuity disclosure must also include a statement that the guarantees of an insurance company are subject to its long-term financial strength and claims-paying ability, as well as an Internet website address to lead participants and beneficiaries to additional information. This information must also be provided in a comparative chart, or a similar format.

The final rule also contains a special provision for plans that offer employer securities ("employer stock"). The rule provides that in place of information regarding principal strategies and risks, the plan administrator must provide each participant and beneficiary with an explanation of the importance of a well-balanced and diversified portfolio. This special rule also describes the circumstances where certain investment-related information (e.g., portfolio turnover rate, fee and expense information, total annual operating expenses, the total annual operating expenses expressed as a dollar amount for a \$1,000 investment) may not be applicable to employer stock.

Following a participant or beneficiary's investment in a designated investment alternative, plan administrators must furnish any materials provided to the plan relating to the exercise of voting, tender and similar rights, to the extent those rights are passed through to participants and beneficiaries under the terms of the plan.

Upon request, the participant or beneficiary must also be provided:

- A prospectus (or SEC approved short form or summary) or the equivalent for unregistered securities;
- Copies of financial statements or reports;
- A statement of the value of a share or unit of each investment, as well as the date of valuation; and
- A list of assets comprising the portfolio of each designated investment alternative that constitutes plan assets and the value of each such asset or its proportion of the investment alternative.

Note that once these rules take [effect](#), plans that are intended to be ERISA 404(c) plans will no longer have to automatically provide prospectuses.

### **Applicability date and next steps**

The final rules will apply to participant-directed defined contribution plans covered by ERISA for plan years beginning on or after November 1, 2011 (e.g., January 1, 2012 for calendar year plans). Initial disclosures must be provided to existing participants and beneficiaries within 60 days after the first day of the first plan year beginning on or after November 1, 2011.

Prudential Retirement is currently analyzing these rules to determine potential changes or additions to existing disclosures. We will provide additional information regarding Prudential Retirement's support of these disclosures well in advance of the applicability date.

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