

New Department of Labor Disclosure Requirements

Part II

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Part I of this article, in the September 2008 issue of *PEO Insider*, available to members at www.napeo.org, covered final rules for Form 5500 Schedule C and proposed regulations amending requirements for the application of Employee Retirement Income Security Act of 1974 (ERISA) 406(b)(2) exemption.

Fiduciary Requirements for Disclosure in Participant-Directed Account Plans

The final of the three sets of disclosure regulations is aimed at improving fee information directly to participants. One welcome change is that the regulations replace the confusing participant disclosure provisions in the ERISA 404(c) regulations, which among other things, required dissemination of the prospectus for each investment a participant selected, a costly and mostly futile exercise because most participants did not read them.

The proposed regulation is being issued under section 404(a), ERISA's prudence and loyalty provisions, with conforming amendments to the section 404(c) regulations. Under the regulations, plan fiduciaries must comply with these new disclosure requirements as a matter of discharging their fiduciary obligations to plan participants. In general, the regulations provide that plan fiduciaries must ensure that participants and beneficiaries, on a regular and periodic basis, are made aware of their rights and responsibilities with respect to their investment selections and provided with sufficient information regarding designated investment alternatives available under the plan, including plan fees and expenses, so they can make informed investment decisions.

The disclosures are broken down into two categories: plan-related information and investment-related information. The plan-related disclosures consist of three sub-categories: general plan information; administrative expense information; and individual expense information.

Plan-Related Disclosures

General Disclosure Requirements

These disclosures must be made to an individual on or before the date she becomes eligible to be a participant or beneficiary under the plan and at least annually thereafter. The general plan disclosures may be made in the plan's summary plan description and include information on the following issues:

- An explanation of how participants may give investment instructions;

- An explanation of limitations pertaining to giving investment instructions, including restrictions on transfer to or from a designated investment alternative;
- An explanation about the exercise of voting, tender, and similar rights related to investments;
- A description of the designated investment alternatives; and
- An identification of any designated investment managers to whom participants and beneficiaries may give investment directions.

In addition, participants and beneficiaries must receive a description of any material changes to the required information not later than 30 days after the date of the adoption of such changes.

Administrative Expenses

On or before the date of eligibility, and at least annually thereafter, a fiduciary must provide participants and beneficiaries an explanation of any fees and expenses for plan administration, e.g., legal, accounting, recordkeeping, that are not included in investment-related expenses and that may be charged against the plan as a whole. Fiduciaries must also provide information about the basis upon which such charges will be allocated to, or affect the individual account balances of participants. This information may be provided in the plan's summary plan description. In addition to these general disclosures, the proposal also requires that, at least quarterly, participants be furnished statements of the dollar amounts actually charged during the pre-

ceding quarter and a general description of the services provided for those fees.

Individual Expenses

On or before the date of eligibility, and at least annually thereafter, a fiduciary must disclose to individual participants charges assessed on an individual-by-individual, rather than plan-wide, basis. These include, for example, expenses related to qualified domestic relations orders, a participant loan, or investment advice services. On a quarterly basis, the proposal also requires that participants be furnished statements of the dollar amounts actually charged during the preceding quarter and general description of the services provided for those fees.

Investment-Related Disclosures

Investment-related disclosures are divided into two categories: automatic disclosures and disclosures based on participant request. On or before the date of eligibility, and at least annually thereafter, the fiduciary must automatically disclose to participants: information identifying the designated investment alternatives; performance data; benchmarks; and fees and expenses.

Identifying, Performance, and Benchmark Disclosures

Identifying information must include: the name of the designated investment alternative; an Internet Web site that supplements the designated investment alternative with information about the investment's issuer or provider, principal strategies and attendant risks, the assets in the portfolio, turnover, and performance and related fees; the category of the investment, e.g., money market, stocks, large or small cap funds; and the type of management used, e.g., passively or actively managed.

Performance disclosures for investment alternatives whose returns are not fixed include information about the average annual total return of the investment for the following periods, if available: one-year, five-year, and 10-year, measured as of the end of the applicable calendar year. The statement must also indicate that an investment's past performance is not necessarily an indication of future

in a nutshell

- One welcome change is that the regulations replace the confusing participant disclosure provisions in the ERISA 404(c) regulations, which among other things, required dissemination of the prospectus for each investment a participant selected, a costly and mostly futile exercise because most participants did not read them.
- In general, the regulations provide that plan fiduciaries must ensure that participants and beneficiaries, on a regular and periodic basis, are made aware of their rights and responsibilities with respect to their investment selections and provided with sufficient information regarding designated investment alternatives available under the plan, including plan fees and expenses, so they can make informed investment decisions.
- Irrespective of how the two proposed regulations get modified when finalized, the future is more transparency and disclosure. All service provider contracts will have to be reviewed to ensure compliance with the new 408(b)(2) regulations and all participant communications will also need to be reviewed.

performance. The name and returns of an appropriate broad-based securities market index over the same periods comparable to the performance data must also be provided. The comparable benchmarks come from unaffiliated investment providers.

Investment-Related Fee and Expense Disclosures

For investment alternatives with respect to which the returns are not fixed, the following disclosures are required:

- The amount and description of each shareholder-type fee, such as sales loads, sales charges, deferred sales charges, redemption fees, surrender charges, exchange fees, account fees, purchase fees, and mortality and expense fees;
- The total annual operating expenses of the investment expressed as a percentage; and
- A statement indicating that fees and expenses are only one of several factors participants should consider when making investment decisions.

The information described above must be provided in a chart or similar comparative format designed to facilitate a comparison of costs for each designated investment alternative.

Information Provided Upon request

Fiduciaries must provide the following information upon request:

- Copies of the prospectuses;
- Copies of financial statements or reports of the investment alternatives to the

extent such materials are provided to the plans;

- Statement of the value of a share or unit of each designated investment alternative as well as the valuation date; and
- List of assets comprising the portfolio.

Under the regulations, these disclosures may be provided through the plan's summary plan description or some other more appropriate form provided that the disclosures are made in a manner calculated to be understood by the average participant.

Summary

Irrespective of how the two proposed regulations get modified when finalized, the future is more transparency and disclosure. All service provider contracts will have to be reviewed to ensure compliance with the new 408(b)(2) regulations and all participant communications will also need to be reviewed. Complying with these new disclosures will add costs to administering plans, but the alternative of falling behind on these new rules when final will be more costly if the Department of Labor finds a violation.●

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