For Transparency's Sake

Forthcoming regulations from the Labor Department will require HR to ensure that employees are fully informed about the fees within their retirement plans.

By Larry Karle

For many of us, summer is a time to relax, maybe hit the beach or the golf course and enjoy an outdoor barbecue. For the U.S. Department of Labor, the early part of the summer was spent putting a framework around fee-disclosure regulations as they pertain to qualified retirement plans. Most experts

agree that this is a giant step in the right direction, considering that the goal is to establish rules around fairness and transparency relating to retirement-plan fees.

Even so, important questions linger: What do the regulations mean for plan sponsors and fiduciaries? How do you prepare for what is coming and, more importantly, make sure that you and your plan are not exposed?Finally, will these new regulations be enough, or should you be doing more for your participants to help them stay informed?

It's critical to note that at this point, the regulations that were framed over the summer are slated to take effect on July 16, 2011 for any defined-contribution or defined-benefit plan qualified under the Employee Retirement Income Security Act.

It should also be noted that these regulations represent Phase 1 of a two-phase initiative. Phase 1 focuses primarily on disclosure to the plan fiduciaries, while Phase 2 -- expected sometime this fall -- will focus on disclosure to plan participants.

Logically speaking, it can be argued that fiduciaries who've thoroughly familiarized themselves with Phase 1 should have a much easier time complying with Phase 2. However, if you have a hard time with the former, you could have a potential human resource crisis of trust between you and your employees on your hands.

Who's Getting What?

The message to plan fiduciaries from this first set of regulations -- not to mention some recently decided court cases -- is that if you do not fully understand who (on the provider side) is getting paid, how much they're getting paid, what they're getting paid for and whether the fees are competitive as they relate to your retirement plan(s), you have until July 2011 to figure it out.

Also, the regulations will require that you must receive the disclosure in writing. Failure to comply could result in a prohibited transaction under ERISA and subject the violator to prohibited-transaction taxes and DOL enforcement actions.

In order to better prepare yourself as a fiduciary, let's take a look at what the regulations say, and then apply them -- from a practical standpoint -- to your role as a plan sponsor and fiduciary.

Current regulations under the "prohibited transactions rules" of Section 406 of ERISA state that the furnishing of goods, services or facilities between a plan and a party of interest is prohibited. If the regulations stopped there, it would mean that many service arrangements between entities -- such as record keepers, third-party administrators and advisers -- and the plan would most likely be judged as being in violation of Section 406.

However, Section 408(b)(2) provides relief from this rule -- as long as the arrangement is reasonable, the services are necessary for the establishment and operation of the plan, and no more than reasonable compensation is paid for the services. In many cases, it's easy to justify services that are necessary, but it's a much different exercise when determining what is reasonable for the services.

Where to Begin?

The first step is to honestly ask yourself, "Do I know everyone who gets paid -- either directly or indirectly -- from the plan, and the amount that each of them is paid?" Even if you feel the answer is "Yes," you should contact your vendor or service provider (record-keeper, TPA) and ask them to provide you with a fee or expense disclosure.

If you have a plan adviser, you should ask him or her to gather the information for you. Many vendors already have this information available, but will only provide it upon request. It is critical to request the disclosure in writing as the new regulations will require this disclosure in writing going forward.

While you are waiting for the disclosure, make a list of people you know who are associated with the plan and get paid for working on it.

Typically, this would include the record-keeper, the TPA (if applicable), investment managers, plan auditors (for plans with more than 100 participants) and brokers or advisers. Make sure that, when you receive the disclosure, everyone you have on your list is accounted for.

If someone isn't accounted for, contact him or her to see why. For example, the vendor's disclosure may not include the compensation paid to the adviser if your company pays the adviser directly. While there are no issues with such an arrangement, it must be included as part of your analysis per the new regulations.

Crucial Credibility

The next question that must be answered, according to the DOL, is whether the plan's fees and expenses are reasonable. Although Part 1 of the exercise should be relatively simple, the second part may prove more difficult -- although, in the eyes of the DOL, it's arguably more critical.

When we go shopping for big-ticket items, we tend to be very sensitive as to what we're paying. It could include the purchase of a home or perhaps an automobile, a boat or even a vacation. No matter the item, it's safe to say that we do a prudent amount of due diligence around the item to ensure that we're getting the best value for our hard-earned dollar.

That same exercise is what the DOL would like you to be doing for your participants -- making sure they are getting the best value for the services that they're being charged for -- which ultimately affects their retirement savings. While nobody would dispute that this due diligence is a good idea, the problem is that there is no "Kelly Blue Book" for retirement plans.

So where can fiduciaries turn in order to cover both themselves and their participants?

One way to approach the process is to hire a third party, professional retirement-plan adviser. The adviser should be one that is not at all affiliated with the plan in any capacity so that the plan can be reviewed without any prejudices.

Consider the recent case that was settled last year (for more than $16 million) between Moline, Ill.-based Caterpillar Corp. and a group of the participants in the company's 401(k) plan who alleged breach of fiduciary duties. One of the issues at hand was that Caterpillar had never engaged the services of an independent party to review and benchmark the plan's fees and expenses.

As part of the settlement, the company agreed to retain the services of an outside firm to monitor the plans during the two-year settlement period.

When it comes to retaining a third-party adviser, you have a number of options: You can retain the adviser on an ongoing basis or, if you prefer, retain it on a project basis to benchmark the plan. Either way, it is the independent nature of the adviser that will add some crucial credibility to the benchmarking exercise.

Once you have the information, it will be critical between now and next July to address any gaps or issues that were uncovered through the benchmarking exercise. Make sure you understand every part of the benchmarking study and how it relates to your participants.

Next, ask your plan vendor or record-keeper what they are working on as it relates to disclosure to participants.

As that phase of the regulations moves forward, it will be important for you to know what your participants will see so you can answer any questions that they may have with the confidence that you have fulfilled your fiduciary obligations on their behalf.

If your plan adviser or record- keeper provides participant education, ask them to include this as part of that education. It will serve to build greater trust and understanding between you and your employees, and build confidence that you are providing a quality benefit for their retirement goals.

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