

Uncovering and Understanding DC Plan Fees and Expenses

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Impact on Participants

- Affects investment return
- Impacts participant retirement

Impact on Fiduciaries

- Fiduciary duty to act prudently and to discharge obligations solely in the interest of participants and beneficiaries

Duties

- Duty to know and understand the fees associated with each investment alternative
- Duty to ensure plan expenses are reasonable in light of the level and quality of services
- Duty to monitor fees charged by investment alternatives to determine if the fees remain appropriate for the level and quality of services provided

Duty of Prudence

- Fiduciaries must discharge their duties prudently
- The exercise of prudence requires a deliberative process
- Fiduciaries must make decisions that that are as well informed as possible under the circumstances.

Process

- Establish a prudent process for selecting, monitoring, and eliminating investment alternatives
- Fiduciaries should document their decisions
- Fees are only one part of the process

Understand the Services Provided for the Fees Charged

- Administration
- Investment services
- Participant education

Suitability

- Ensure the fees may be charged to the plan

Fee considerations

- Compare the services received with total cost
- Compare fees charged by investment alternatives with similar characteristics
- Request ongoing fee information
- Understand that cost is only one consideration

Fee considerations

- Understand how fees are paid
 - Charged to the plan
 - Deducted from investment returns
 - Included in base fee or additional charge
 - How additional charges are calculated
 - Charged upon occurrence of particular events

US Fee Disclosure Regulatory Regime

- Tripartite Approach
 - Plan reporting requirements – effective 2009
 - Service provider disclosure to plan fiduciary – effective July 1, 2012
 - Participant disclosure – effective August 31, 2012

Plan Reporting Requirement

- Plan service providers who receive \$5,000 or more in direct or indirect compensation must be identified
- Compensation includes money or thing of value
 - Thing of value includes gifts, awards, trips

Direct Compensation

- Payments out of a plan account
- Charges to plan forfeiture accounts
- Charges to a plan's trust account before allocations are made to individual participant accounts
- Charges to individual participant accounts
- Does not include charges paid by the plan sponsor

Direct Compensation

- Bundled service arrangements priced as a package
 - Unless payments are made on a per transaction basis
 - Do not need to be allocated among affiliates or subcontractors

Indirect Compensation

- Fees and expense reimbursements received by a person from the investment or financial institution offering the investment

Examples of Indirect Compensation

- Recordkeeping fees
- Asset-based management fees
- Finder's fees
- Float revenue
- Brokerage commissions
- Fees for participant education
- Fees for filing the plan's tax return
- Not insurance premium payments
- Not attorney and accountant fees

Service Providers Who Fail or Refuse to Provide Information

- Must be identified

Service Provider Disclosure

- Policy goals
 - Fiduciaries are able to evaluate the reasonableness of direct and indirect compensation received by service providers
 - Fiduciaries are able to identify potential conflicts of interest
 - Reporting and disclosure requirements may be satisfied

Application of Service Provider Disclosure

- Applies only to pension plans
- Rules for health plans to be developed
- Threshold amount of \$1,000 per year

Direct Service Providers

- Compensation received from the plan
 - Fiduciaries
 - Investment advisers
 - Platform providers
 - Disclosure required from entity in contract with the plan in bundled arrangements.

Indirect Compensation

- Compensation received from any source other than
 - Plan
 - Plan sponsor
 - Covered service provider or any affiliate

Indirect Service Providers

- Service Providers who also receive indirect compensation
 - Accounting
 - Auditing
 - Banking
 - Consulting
 - Custodial
 - Insurance
 - Investment advisory
 - Legal
 - Recordkeeping
 - Securities Brokerage
 - Third Party Administration
 - Valuation Services

Service Provider Disclosure

- Furnished in writing to plan fiduciary (may be electronic)
- Must describe all services to be provided by the service provider and its affiliates and subcontractors
- Must describe any allocation among related parties if charges are made against a plan investment or per-transaction basis
- Record keepers must disclose compensation attributable to recordkeeping even if no charge is identified in the contract
 - May be an estimate
- Must provide reasonably in advance of the date the fiduciary requires the information.

Indirect Compensation

- Must describe all indirect compensation arrangements to permit the fiduciary to evaluate conflicts of interest
 - Source of indirect compensation
 - Services provided in exchange for indirect compensation

Updates

- As soon as practicable, but no later than 60 days after service provider learns of the change
- Investment-related information must be updated at least annually
- Errors must be corrected within 30 days after service provider learns of the error

Participant Disclosure

- Plan-related information
 - General plan information
 - How to give investment instructions
 - Current investment alternatives
 - Administrative expense information
 - Expenses to be deducted from all individual accounts
 - Individual expense information
 - Expenses related to the individual's actions

Timing of Plan-Related Information Disclosures

- Eligibility date
- Annually
- Quarterly report of plan-related charges to the participant's account

Participant Disclosure

- Investment-Related Information
 - Chart format
 - Performance Data
 - 1, 5, 10 year return or annual rate of return and term
 - Benchmark Information
 - 1, 5, 10 year comparison with market
 - Fee and Expense Information
 - Total annual operating expenses as a percentage of assets and as a dollar amount for each \$1,000 invested and purchase and withdraw restrictions

Investment-Related Information

- Internet Web Information
 - Additional information
- Glossary

Timing of Investment-Related Information Disclosures

- Eligibility date
- Annually